CHECK AGAINST DELIVERY

The Economic and Fiscal Update

A Presentation by
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Canada

Mr. Chairman, I would like to thank you for your invitation to be here this afternoon. I have followed your consultations with Canadians across the country with great interest – And as a result, I look forward to your report with much anticipation.

In October last year, when I appeared before this Committee to provide an update on the state of our economy, I outlined the unprecedented challenge before our country.

We talked about the necessity of increasing economic productivity – and restoring health to our public finances. And we discussed the need to restructure the role of government.

Following our discussions, in last February's budget, substantial progress was made. We are well down the road. But it must be emphasized we are not yet at our destination.

Prior to reviewing the challenge that lies ahead, let me re-iterate one fundamental point.

Our objective is not simply a better balance sheet. Nor is our goal limited to more effective government.

It is a better country. It is a fairer society. And it is an economy that – more than anything else – is capable of producing the kind of jobs and growth that will enable Canadians to believe in themselves and to have faith in their future.

To get there, we believe government must pursue two tracks – simultaneously and with determination.

The first is to address the macro-economic fundamentals.

That means continuing our firm policy to sustain low inflation. And it means continuing our strategy to clean up the nation's finances.

The second track is to get the structure of the economy right. And to do that, we must get the structure of government right. A government that knows where it can – and where it must make a difference. A government focussed as never before on key national priorities.

Pursuing these two tracks is not a temporary challenge, some one-year task. The very essence of economic and government renewal is that it is dynamic, that it never slows down. In our 1994 budget, we set the stage. In our 1995 budget, we set the course. In the budget that lies ahead we must keep on course. We must consolidate our achievements. We must build further on the foundation we have laid.

We must continue to forge ahead.

Today, there are some who doubt our resolve. There are those who say we won't stay the course. There are others who say we shouldn't. They are mistaken. Too much is at stake to stand still. Too much has been accomplished to let up.

Those who would have Canadians believe that there is a contradiction between deficit reduction and job creation are simply wrong. Continued deficit reduction is essential if we are to get interest rates down – interest rates that stand in the way of the creation of jobs.

For this reason, our determination to restore fiscal health will not falter.

As in the past, we will meet our targets using prudent economic assumptions. And we will set aside a substantial contingency reserve.

Let me now deal briefly with the state of our economy as it has evolved since the last budget.

Last February, we projected an economic slowdown, as higher interest rates weakened the U.S. economy. But the fact is that slowdown came much sooner than economists anticipated and was much more pronounced than they had predicted.

However, today as we speak, the signs are more promising.

The U.S. economy is poised for moderate expansion through 1996 and beyond – which is good news for Canadian jobs and growth.

Domestically, interest rates have been falling – down almost 2½ percentage points from their early 1995 peaks. Analysts widely agree that this is partly in response to the action we took in our last budget.

And although interest rates shot up during the referendum campaign, they returned to previous levels in the aftermath of the result. That being said, they are still too high.

Nobody can deny the tremendously damaging effect political uncertainty has on economic confidence and growth.

If today we are talking about stimulating job creation – through the pursuance of sound economic policy, no one should be under any illusion as to the costs imposed on our economy, on every Canadian, by political uncertainty.

Since this government came into office, about 450,000 new jobs have been created – all full-time – and the unemployment rate has fallen by 1.7 percentage points.

Real GDP was up by 2.1 per cent in the third quarter of this year.

That being said, we're not out of the woods yet. For instance, after three consecutive good months, employment numbers for November were disappointing. What that demonstrates is that we can not let up. And we are not.

Our cost competitiveness continues to rebound strongly vis-à-vis the United States. It is the best it has been in the entire 45 years that data have been available.

Our merchandise trade balance, exports over imports, at $34.6 billion, was at an all-time high in September. As a result, relative to GDP, our current account deficit has fallen to its lowest level in ten years, thus slowing the build-up of our foreign debt.

Our economic fundamentals are strong. The challenge is to keep them strong – to take the budgetary action that will translate those basic strengths into more jobs for Canadians.

It is widely agreed that the 1995 budget made very real progress. However, it also made even more clear what our priorities must be in the future.

Let me begin with the fiscal challenge.

Our fundamental problem remains a debt that is growing faster than our economy. Now you can approach this 14 different ways to Sunday, but there is only one solution and that is an economy that is growing faster than our debt. In short, we've got to stop the growth of our debt and increase the growth of our economy.

For economists, the relationship between the growth in our debt – and the growth of our economy – is captured by a key ratio: debt-to-GDP i.e. the level of our debt (what the nation owes) as a percentage of our gross domestic product (what the nation produces). Over the past two decades, that ratio has been rising, relentlessly.

All of us know the nature of the relationship between what we earn and what we owe. When we owe a great deal of money, we know that the worst thing to do is to go out and borrow even more. But we also know that making payments would be easier if we were able to earn more money. In fact, we know that the best strategy of all is to both limit our personal borrowing and increase our income. That is precisely our challenge as a country.

Twenty years ago, for the federal government, the debt-to-GDP ratio stood at 19 per cent. Ten years ago it stood at 50 per cent. Today, it is close to 75 per cent.

Over the years, there were those who said that economic recovery would suffice to turn the situation around. Well, we have always said they were wrong. The fact is in times of recovery, the problem didn't get better – and in every downturn, it got worse.

There are also those, who declare that the only answer lies in cutting government spending. Well, they too are wrong – because they ignore the reality that the social deficit, the technological deficit – are central to the financial deficit. The issue is not simply excessive government spending.

The very nature of a ratio is that it is a relationship between two variables.

The debt-to-GDP ratio reveals the two things on which we must concentrate.

One is to keep our spending under firm control. The other is the necessity to maximize the nation's potential, its productivity, its capacity to grow, to create jobs. The debt is about what we owe. The GDP is about what we do.

The logic is clear. Yes, governments must cut their spending in order to bring their deficits down. But as well, in an economy that is growing, incomes grow – increasing the revenue that governments get. That also brings their deficits down. And in an economy that is growing, jobs are created – decreasing the need for governments to spend more. And that also brings deficits down.

To focus on economic growth and jobs is not to ignore the debt-to-GDP problem. In fact, it is an essential part of the answer.

Our strategy must be based on synergy. Neither growth nor deficit reduction is sufficient alone. But pursued together, they can do the job.

This brings me to the steady pace approach we have adopted right from the beginning.

There is no doubt that if our only priority as a government was to get the deficit down to zero immediately, that could be done – in theory. But it would be very damaging in practice.

Our goal is not simply to get the deficit down, it is to keep it down. That requires considered and careful reform – and implementation. That is something a slash and burn approach precludes – something a measured strategy assures.

But the issue goes beyond that. We believe there are things that a responsible government must provide to its citizens. Hard fiscal times require hard choices. A zero deficit? Yes, that will be achieved. But we simply refuse to get there by leaving Canadians behind.

This is a question of values – but it is also a question of sound economics. Mindless cuts – without concern for the consequences, or the need for adaptation – may result in short-term savings. But they can also result in substantial long-term costs.

For example, in our unemployment insurance reform, just announced, we could have achieved more savings in the short-term by focussing only on lowering the benefits – without giving Canadians the tools to help them get back to work.

But where would that leave Canadians who want a job?

It would mean more hardship, a weaker economy – and much greater spending pressures in the end.

We could abandon our tax preferences for small business. In the short term, the government's revenues would go up. But in the long term, there would be less innovation – and fewer companies. The result would be lost income and lost jobs – and, in fact, greater pressures to spend in the future.

We could shut down our program for export assistance. Money would be saved. But if we lose exports, Canadians lose jobs.

The point is: a single-minded dash to a zero deficit would be counterproductive in every sense. What we are pursuing is a strategy that is measured, that is deliberate, that is responsible. That is the course we set out in the Red Book. And that is the course we are on today.

Now, meeting the debt-to-GDP challenge may sound to many Canadians like a priority for economists – or Finance Ministers – not for them. Unfortunately, nothing could be further from the truth. All of us pay the price of government deficits and debts. And all of us will realize the benefits once that burden is lifted.

Why? Look at the facts.

Only 20 years ago, 11 cents of the federal revenue dollar went to pay the interest on our debt. Today, it eats up 36 cents of every dollar sent to Ottawa.

Canadians want their tax dollars to be used for services and programs for them. If those services and programs are to be available in the future, we simply must act now to reverse the growth of the debt-to-GDP burden.

There is a second reason to act as well – for many even more compelling than the first. Our debt-to-GDP ratio is such that it is a damper on jobs and on growth.

Why? Because it keeps tax rates too high; it pushes interest rates up; and it discourages savings and investment.

High interest rates exact a terrible cost – on households, on investment, on consumer confidence, on jobs.

What is the connection between this and the nation's balance sheet?

It is the fact that it is the rates of interest national governments must pay – that ultimately determine the rates of interest citizens must pay.

Consider the impact.

Two additional percentage points of interest on a $100,000 mortgage means $1,600 per year in extra payments. That is money that cannot go to purchase goods and services. That means fewer jobs.

This chart makes a compelling case.

Between last November and January this year, one year mortgage rates went up from 8 to 10 per cent. So is it then a total coincidence that housing starts fell 10 per cent in the first quarter of this year – and another 15 per cent in the quarter that followed? The result: fewer jobs and lower incomes.

Another example – the effect on small- and medium-sized businesses. A 2 percentage point increase in interest rates would increase the cost of a $2,000,000 business loan by $28,000 per year. That also means lost jobs.

Our bottom line is straightforward. There can be no more effective job creation program by government than to get interest rates down – and there is no more effective way to get interest rates down than to get the deficit down. It is that reality that drives our determination and reinforces our resolve.

For example, recent economic analysis suggests that a 2 percentage point decrease in interest rates woud, over 4 years, make the economy 2¼ per cent larger – to the tune of more than $13 billion.

This represents sales gained by employers, wages paid to new employees and raw materials bought to make new products. This means jobs.

Surely, there can be no more successful job creation initiative by government than to take the steps that will bring those benefits to Canadians. That is what we are doing.

By 1996-97, with our 3 per cent interim deficit target secured, we will have halted the growth of the debt-to-GDP ratio. But that simply sets the stage for the next challenge – which is to ensure that that ratio continues to track downward – year after year, cycle after cycle.

Meeting that challenge means more jobs.

It also means a country whose economic independence and sovereignty is being strengthened, a nation less dependent on foreign lenders – a nation freer to focus on the broad national interest of its people.

Mr. Chairman, it is for all these reasons that this government has mounted the largest assault on the federal deficit in Canadian history. Last month, we announced that the deficit for our first full year in office was $37.5 billion, $2.2 billion below the target set in our first budget – and $4.5 billion below the previous year.

In 1993-94, the deficit stood at 5.9 per cent of GDP. It went down to 5 per cent last year. And this year, the deficit will continue to decline to 4.2 per cent of GDP – on its way to 3 per cent in 1996-97.

Our goal – is to eliminate the deficit. Our approach – is to set a series of rolling two year targets – an approach that we have demonstrated works better than any other. Our progress is clear.

In order to maintain that progress, I am announcing today, that the deficit for 1997-98 will be brought down to 2 per cent of GDP.

This is estimated to be approximately $17 billion.

This means we will have cut last year's deficit by more than half and it also means that the debt-to-GDP ratio will be on a downward track.

Furthermore, this means that the government's new borrowing requirements on credit markets in that year – which is the way many other governments, the United States for instance, calculate their deficit – will be less than $7 billion, i.e. less than one per cent of GDP.

That means that by 1997-98, new borrowing requirements – in relation to the size of our economy – will be at their lowest level since 1969.

Let me turn now to the second track of our jobs and growth strategy. In our view, significant as fiscal measures are, what is as important is the redesign of the very role and structure of government itself.

Restructuring government has been central to our approach from the beginning. It was at the heart of our first Program Review, as it is of Program Review II, currently underway.

In our view, fiscal reform that is durable is possible only through government reform that is structural.

Furthermore, to reduce government spending without redesigning government would be to embody a short-term approach, a quick fix that by its very nature would be fundamentally flawed. It would result in weaker government – government unable to meet the challenges – and take advantage – of the opportunities of our evolving economy, and of our changing society.

At the core of a more effective government must be the recognition that Canada cannot escape – indeed must embrace – the implications of an increasingly global, interdependent world. It is simply a fact of life, as a relatively small but very open economy, there is no more pressing responsibility than to make globalization work in our favour.

This means in areas where only the federal government can provide leadership and direction, its efforts should be enhanced. It also means that in areas where other levels of government are better positioned to serve the needs of our citizens, further reform must occur.

In this evermore interdependent world – when problems intersect, where solutions cross issues and borders, where local realities have global impact – and vice versa – it is more important than ever to recall, and to re-enforce, the very core meaning of federalism itself. Federalism is about dynamism – a dynamism flowing from the flexibility, the experimentation, the adaptability only it can bring. That dynamism is not some accidental by-product. It is one reason federations exist.

And so, we should concentrate on federalism's strongest suit – governments exercising their own jurisdictions on the one hand, and partnerships on the other hand – the coming together to work out joint decisions on joint problems.

That's what the Internal Trade Agreement of 1994 was about. That's what the infrastructure program is about. And that's what the Team Canada trade missions led by the Prime Minister – to China, to Latin America, and next to India – are about.

There is another question as well we must ask – and that is whether in some cases government at any level is the answer. In our view, governments should focus on what they can do best – and leave the rest for those who can do better – whether business, labour or the voluntary sector.

That philosophy, for example, lies behind the privatizations – first of Petro Canada, more recently of CN, and in the future of the Air Navigation System.

What should the national government do? It should focus on key national priorities.

What does that mean?

Well, among other things – it means jobs.

It means making the improvements to unemployment insurance system that are the most profound in the last 25 years, bringing it into line with the labour market realities of the 1990s.

It means encouraging small business to invest and to hire, by lessening the regulatory burden, by improving their access to capital.

For example it means giving the Business Development Bank of Canada new flexibility and new lending capacity; and making our regional agencies a single entry point for small business access to government programs.

The jobs priority means strategic support for science and technology – support for programs where the economies of scale are such that only a national approach will work.

In today's fiscal circumstances, we are doing as much as we can. In the future, when the situation is turned around, we must and we will do more.

What are our priorities? They are answering the need for sustainability of our social programs posed by an ageing population and by a changing economy.

This priority is reflected in our unequivocal support for Canada's system of healthcare – support demonstrated by our commitment to stabilize cash transfers to the provinces.

This priority is reflected in our commitment to ensure that Canadians are not discriminated against when they move from one part of the country to another and seek social assistance.

This priority on sustainable social programs is also reflected in our commitment to our publicly funded system of pensions. Our commitment to today's seniors. And our commitment to young people so that when the time comes, the system will be there for them too. A commitment on which we will act.

Now, on these two central priorities – more jobs and better social programs – we would be less than candid today if we pretended we are doing all we would like. The bottom line is that the state of the national pocketbook simply does not make that possible.

That we are in this situation is unacceptable. That we must get out of it is essential, which is what makes deficit reduction and its eventual elimination so necessary – not as an end in itself, but as a means to achieve the nation's greater goals.

Mr. Chairman, let me summarize our course. In 1994 and 1995, this government took the decisions necessary to put this country on a new and better road. The road of fiscal recovery. The road of government renewal. Both of which lead to more jobs and greater economic growth.

We are on track to meet the fiscal targets we have set. Our course is clear.

We are on the right road. The task now is to turn the next corner.

In our third budget, we must build on the progress we made in our first two. We must ensure that the substantial savings from our previous budgets continue to take hold and pay-off for Canadians. We must consolidate our gains. We must ensure that we never fall back.

To conclude, I would like to make one final point. We have talked a lot today in terms of numbers. And yes, we need to get the numbers right to get the nation right.

But none of us are here simply to write new entries in a ledger – to keep better books. We are here to write a new chapter of history – to build a better country. We are a free people founded on diversity, sustained through tolerance, a society that believes that success and civility can and must be secured together.

More than anything else, it is those values that will strengthen us, those values that must guide our economic vision.

The point is, whether from Val d'Or or Fort McMurray, despite our diversity, most of our challenges and all of our opportunities do not differ. On the contrary, we hold them in common.

What are these challenges and the opportunities they present? To create more and better jobs. To create better social programs. To improve the finances of all levels of government.

To succeed in a world where the opportunities are greater than ever – but so too are the risks.

We can have a future second to none – in a country which safeguards the identity and pride of each and everyone of us. How? If we work to build upon the extraordinary values – compassion, tolerance, and ambition – that are our common heritage.

Mr. Chairman, we are a country where tremendous success is ours for the taking. The raw materials we have at our disposal are extraordinary: our foundation, already achieved, as one of the leading nations of the world. Resources – natural and human – that few others can match. Skills that in so many areas are second to none, and a culture that mirrors the diversity of an entire world. It is time to draw these together, to shape them to our advantage for a new century.

While there are differences among us, there is nonetheless a remarkable consensus on the kind of country we want to create.

A country where everyone who is able to work can find a meaningful job. A country where Canadians in need can have confidence that their social programs will be there for them. A country that sets new standards of excellence across-the-board.

It is these goals that must re-enforce our resolve to work together. Mr. Chairman, we talk a lot in this country about creating strategic alliances with others – abroad. Now, more than ever, it is time to form a new strategic alliance – here at home. I now look forward to the discussion with the members of this Committee on how we can do that together.